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HR&BENEFITS UPDATE

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Performance Management: Are Annual Performance Reviews Necessary?

HUMAN RESOURCES

Lately, organizations have begun talking about abandoning the annual performance review. Many managers believe they're not worth the time. Employees complain that they don't get much meaningful feedback from them. Even HR professionals often complain that the performance appraisal isn't effective. Still, most organizations continue to do them, mostly because that's the way things have always been done. However, performance reviews, when done correctly and with thought, can be a useful tool.

Steve, a colleague of mine, told me the story of his performance review last year. Throughout the 12-month review period, Vicky, his manager, who worked in a different state, had spent a very limited amount of time with him. Their scheduled biweekly 1:1 meetings were rarely kept, Vicky had not once traveled to his region in the previous year, and most communication was via email. Steve had met all of his metrics, and his nationwide client retention percentages put him in the top three performing employees. His team often looked to him for advice and guidance, and he was highly thought of within his division. Many clients had also reached out to Vicky, speaking highly of Steve and telling her how fortunate she was to have him on her team.

Steve was given a week to complete his self-evaluation, with a large section of the form focused on metrics. The numbers were something Vicky had easy access to, but she did not offer the data to Steve. It took him many frustrating emails and phone calls to track down these numbers, but he finally got the requested information.

The day of Steve's evaluation, Vicky made the trip to his region. He was excited and nervous because they had spent little time together over the previous two years. The opportunity to grow their relationship had never presented itself. Vicky had also completed the Performance Appraisal form, indicating how she thought he had done over the last 12 months, and he was given a copy.

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Locating Missing Participants

RETIREMENT

At one time or another, all plan sponsors will likely be in the position of having to locate missing participants. This may be related to delivery of regulatory required communications, distributing of assets or communicating fund changes to active and/or terminated participants. If the delivery of necessary communications is encumbered because a participant cannot be located, there exists a fiduciary requirement to perform a "reasonable search" for this "missing" participant. There are various search methods that would be considered reasonable good faith efforts, including:

- Certified mail (with a return receipt) to the last known address
- Checking records of other benefit plans (i.e., employer-provided health plan)
- Using a commercial participant-locating or letter forwarding service (such as www.unclaimedretirementbenefits.com) (Historically the U.S. Department of Labor (DOL) required use of either the IRS or Social Security Administration letter forwarding programs, but both of those programs have been discontinued within the past year; it is a reasonable assumption that the DOL will want to see use of a commercially reasonable equivalent in the absence of those programs.)

In the event that your plan allows cash-out distributions on terminated participants with account balances under $1,000, or rollover to individual retirement accounts (IRAs) for balances between $1,000 and $5,000, be sure to check the provisions described in the plan document. Typically a rollover to an IRA on behalf of these participants can be accomplished for participants deemed missing. For more information on this topic, please contact your plan consultant.

Need more information?

For information on any of the articles in this newsletter, please contact your benefits advisor.

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There was a complete disconnect between Steve and Vicky regarding his performance. He was startled to have received mostly 2s, with a peppering of 3s (on a scale of 5, with 5 being the highest score). When they started diving deeper into the review, the conversation became quite heated.

An example of one of the most significant disagreements was his level of engagement with clients on a strategic level. All of the work Steve had completed with his clients was well-documented in an information system that produced his metrics. He argued that his results told the story of his performance. Vicky, who had not attended a client visit with him in over 18 months, told him that he was too tactical in his work with clients and was not a team player. Vicky also personally attacked the way he looked (she claimed he wore too much black), the way he spoke (he spoke too fast, so she didn't trust him), and the way he was unable to bond with the team. Vicky claimed that no one on the team of 15 liked him, and that they all told her so. As you can imagine, things didn't get any better. Steve finally gave up after arguing with Vicky for nearly three hours. At the end of the review, Steve walked away feeling angry, defeated and completely demotivated.

Did Vicky do anything correctly? Well, she did schedule the review, come up to the region and spent time with Steve, things she hadn't done in a long time. Beyond that, Vicky probably should have managed this performance review entirely differently.

The Right Way

Performance management programs work well when they are meaningful to both the employee and the manager. Waiting 12 months to hear you're doing great, or not so great, is far too long. Scheduling and keeping 1:1s with employees on a weekly, biweekly or even monthly basis will give both the employee and the manager better lines of communication, which will foster honest feedback about performance. These brief, informal performance reviews should let the employee know what he or she needs to continue doing, start doing and stop doing. Without 1:1s, managers are often out of touch with what's going on within their teams, which may lead to poor performance and a meaningless annual performance review.

I believe in annual reviews when the person conducting the review is well trained in the process, and has been engaging and motivating his or her employees throughout the entire review period. I believe that nothing said during the review should come as a surprise to the employee. I also believe that these meetings between manager and employee should be a productive and positive two-way conversation.

Besides the interpersonal component of the performance review, there's also the legal side. The performance review forms become legal documents, and must be completed with care and honesty. Emotions must be left out, and comments must be completely objective.

Because performance reviews are often tied to pay increases, promotions and even layoffs, it's crucial that performance reviews be accurate and fair. Accurate information will back up why a particular employment decision was made. Below are some guidelines to follow to ensure legal compliance:

- Performance appraisals should not be used in a punitive or retaliatory fashion. It is grossly unprofessional for a manager or supervisor to use the appraisal process to "get even" with an employee who has displeased or upset them in some way.
- Appraisals should not be used to discriminate against employees on the basis of race, religion, age, gender, disability, marital status, pregnancy or sexual preference.
- Performance appraisal results should be fair, accurate and supported by evidence and examples. For instance, if an employee has poor interpersonal skills and is harming morale and group performance, the supervisor might keep a written log of incidents. Co-workers may be interviewed and their views and reactions recorded. The nature and effects of the employee's behavior should be documented.
- An employee should have the opportunity to comment on his or her appraisal result and to express agreement with or objection to the performance review.
- Appraisals should be balanced, recording information on both the good and the bad aspects of an employee's performance (as far as possible).
- Appraisal results should not be used as the sole basis for promotion or termination decisions. A broad range of information should be considered, in which the employee's appraisal results may be significant but not necessarily conclusive.
- Retain records. If an employee believes that he or she has been dealt with unfairly, he or she may have a cause of legal action. In the case of poor performers, persons dismissed or demoted, or those who resign or leave in less-than-ideal circumstances, we suggest that appraisal records, together with critical incident logs and other relevant documents, be archived indefinitely. Check with local legal specialists as to required periods of record retention and time limits on the rights of potential litigants, as these vary from one jurisdiction to the next.
- Appraisal results should be treated as private and confidential. Record storage should be secure and controlled. Only people with a legitimate business need to know should have access to an employee's performance appraisal information.
- If an appraisal result is poor (or in any way likely to be controversial or provocative), ask an objective third party for his or her views on whether the appraisal result seems fair and reasonable. Be prepared to modify the appraisal if the second opinion is not supportive of the result.
- Appraisals should avoid inflammatory and emotional language. As far as possible, aim for a detached and dispassionate style. Ensure that criticisms relate to actual job requirements and are not based on mere personal or other irrelevant issues.

Performance management reaches far deeper than just the annual performance review. Performance management is an ongoing process. Research indicates that employees often resign their positions due to the lack of a relationship with the immediate manager, a lack of recognition of their job performance or a lack of advancement or growth opportunities. Be sure to give employees continuous feedback throughout the year, and don't be reticent to tell them how they're doing.

Establishing Your Retirement Plan Committee Charter

RETIREMENT

As retirement plan consultants, we strongly encourage our clients to formally establish a retirement plan committee. The establishment of a committee may be formalized by adopting a retirement plan committee charter. This committee charter helps to protect the named fiduciary, typically the board of directors, by delegating certain identified fiduciary responsibilities to the committee. It protects the committee members by defining the specific duties for which they are responsible. Furthermore, it protects the participants, as it provides for orderly and prudent governance of the plan designed for the exclusive best interests of the participants and their beneficiaries, as required by ERISA Section 404(a).

Discuss this topic with your plan consultant during your next meeting. He or she can assist the process of adopting a committee charter by providing our sample committee charter document and helping select the appropriate provisions. Consider the following discussion points:

- Determine the purpose of the committee (investment-related, administrative issues, or both).
- Determine how committee members are selected (who should or should not be members).
- Is there an ideal number of committee members?
- What topics should the committee cover?

The recent volatility in the stock market, combined with our litigious society, is generating concern on the part of many fiduciaries regarding their potential exposure. Taking a casual approach to plan governance, without a formalized committee charter, will not help insulate the company or the plan fiduciaries from participants' complaints or lawsuits. Call your plan consultant for more information.

Compliance FAQ

How must health flexible spending arrangements (FSAs) be structured to meet the definition of "excepted benefits" under HIPAA and PPACA? How does that interact with PPACA's $2,500 limit on employee contributions to a health FSA?

Central to this issue is that health FSAs must be structured as HIPAA-excepted benefits to avoid the PPACA requirement that employer-sponsored group health plans – including health FSAs – cover all preventing services at zero cost-sharing for the employee. The preventive services requirement applies for plan years beginning on or after Jan. 1, 2014, and therefore health FSAs must meet the excepted benefit definition by that date, or risk penalties.

To qualify as excepted benefits, the FSA must satisfy two conditions:

1. **Maximum benefit condition.** This condition requires that the maximum benefit payable under the health FSA to any participant in a class for a year not exceed two times the employee's salary reduction election under the health FSA for the year (or, if greater, the participant's salary reduction plus $500).
2. **Availability condition.** Under this condition, other non-excepted group health plan coverage, such as major medical coverage, must be made available for the year to the class of participants eligible for the health FSA by reason of their employment.

Regarding the maximum benefit condition, an FSA funded solely by employee salary reductions will automatically satisfy the maximum benefit condition, because the maximum benefit payable could never exceed the employee's salary reduction election, let alone exceed it by two times.

If the employer contributes to the FSA, however, the maximum benefit payable under the health FSA (the sum of employer and employee contributions toward the FSA) must be measured to determine if that maximum exceeds two times the employee's FSA salary reductions.

Here are several examples of health FSA funding that meet or do not meet the maximum benefit condition:

Examples of Health FSA Funding That Meet the Maximum Benefit Condition:
Any one-for-one employer match (e.g., employer $600, employee $600)
Any employer contribution of $500 or less (e.g., employer $500, employee $200)
Examples of Health FSA Funding That Do Not Meet the Maximum Benefit Condition:
Any employer contribution of more than $500, if employee contributes $500 or less (e.g., employer $600, employee $400)
Any employer contribution in excess of one-to-one match, if employee contributes more than $500 (e.g., employer contributes $700, employee contributes $600)

Regarding the availability condition, if all employees who are eligible for the health FSA are also eligible for major medical coverage (whether or not they enroll), the health FSA would be considered HIPAA excepted. If the eligibility provisions under the health FSA are such that more employees are eligible for the health FSA than for the major medical coverage, then the availability condition may not be met.

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$2,500 Employee Contribution Limit for Health FSAs

As background, PPACA generally limits employee contributions to a health FSA to $2,500 annually, as outlined in Internal Revenue Code 125(i)(1). Here are some quick notes on the limit:

- The limit applies regardless of grandfathered status.
- The limit relates only to employee contributions, meaning that non-elective employer contributions to the FSA are not counted toward the $2,500 annual limit.
- If employees can elect to receive employer contributions to their health FSA as cash or as a taxable benefit (generally done through a Section 125 plan), then the contributions are considered employee salary reductions and would be counted toward the $2,500 annual limit.
- In the case of married couples, each spouse can contribute up to $2,500 to a health FSA, even if both spouses work for the same employer and participate in the same health FSA. Also, an employee that is employed for two different employers (not of the same controlled group) may elect up to $2,500 under each employer's health FSA.
- The $2,500 limit applies regardless of the health FSA's HIPAA-excepted status. Thus, to avoid PPACA penalties, employers will need to structure their health FSAs as HIPAA-excepted benefits by adhering to the maximum benefit and availability conditions, and by limiting employee contributions to the health FSA to $2,500 each plan year.

Employers may need to amend cafeteria plan documents to reflect the changes, and amendments should be carried out according to the plan amendment procedures described in the plan document. Generally, amendments to cafeteria plan documents must be made before implementing the change. However, the IRS has stated that an amendment to adopt the $2,500 limit may be adopted retroactively, so long as the amendment is adopted on or before Dec. 31, 2014.

- Employers should work closely with their advisors in ensuring health FSA compliance.

For more information on any of the articles in this newsletter, contact your benefits advisor.